

**Michigan Department of Education
Office of Financial Management**

**Local School Districts
Indirect Cost Rate Instructions
May 2004**

What are indirect costs?

Indirect costs are defined as costs that are incurred for the benefit of more than one cost objective, but are not readily assignable to any program. Indirect costs serve common or joint purposes, and to identify the specific program or project served would take an effort disproportionate to the results achieved. Typically, salaries and expenses for auditing, budgeting, payroll, personnel, purchasing and employee relations are examples of costs which are considered to be indirect costs.

What is an indirect cost rate and why should my organization be interested in obtaining an approved indirect cost rate?

An indirect cost rate is a ratio, based upon the costs of all operations of the organization, which proportions indirect costs to direct costs. Direct costs are defined as those costs which are readily identified with a grant, contract, project, function or activity. The total direct costs of any grant or activity can be multiplied by this indirect cost ratio, thus providing a reasonable approximation of the indirect costs of that grant or activity. The full cost of the activity includes both the direct costs and the indirect costs assigned via the indirect cost rate. For example, if your organization has a 4.0% indirect cost rate and spends \$48,000 in salaries, benefits, travel and supplies for a specific program, it can be assumed that it costs an additional \$1,920 to provide services such as payroll processing, human resource management, supply requisitioning, etc. to the program. The complete cost of the program is \$49,920.

When an organization has an approved indirect cost rate, it is allowed to assign a value for indirect costs to grants or projects. In the majority of grants, it is permissible to request reimbursement for both direct and indirect costs to the extent of the grant award. Your organization may be able to increase the dollars recoverable on grants by using an approved indirect cost rate.

What is the process for obtaining approved indirect cost rates?

The Office of Financial Management sends form R0418, via traditional mail, to each district in the spring. Form R0418 contains a recap of the district's financial data from the preceding fiscal year on which the following fiscal year's preliminary indirect rates are based. Form DS-4513 is used to adjust and improve the data on the R0418 so the rate accurately represents the operations of the district.

Form DS-4513 *LOCAL SCHOOL DISTRICT: INDIRECT COST RATE ADJUSTMENTS* and instructions are available on-line. To access the DS-4513 and instructions, go to

www.michigan.gov/mde, click on the following:

“Programs and Offices”, then

“Financial Management”, then

“Financial Management and Administrative Services”, then

Under “Resources and Related Information”, Federal Indirect Cost Rate Development Section”, then

“2004-2005 Local District Indirect Cost Rate Instructions” and “DS-4513 Local School District: Indirect Cost Rate Adjustments Form”

Instructions for completing DS-4513 for 2004-2005 indirect cost rates:

1. Verify the data on the R0418: The expenditure information provided on form R0418 represents fiscal year 2002-2003 Form B data. (Note that only food service expenses are included in the School Service Fund column.) Indirect and direct cost information provided on the Carryforward Calculation has been extracted from the Carryforward Calculation section on the R0418 for the 2002-2003 indirect cost rates. Please verify the accuracy of the data. Contact Lori Schomisch at (517) 335-0539 if the information is not correct.
2. Determine the Need for Adjustments: Preliminary Report R0418 classifies expenditures as indirect restricted, indirect unrestricted or direct costs based upon the typical classification of expenditures represented by the account. The classification may or may not be accurate, depending upon the expenses reflected by the value. The purpose of form DS-4513 is to report adjustments to the expenditure classifications to accurately represent the district’s ratio of indirect costs to direct costs.

It is not mandatory that you adjust the preliminary information. If the amounts recorded on report R0418 are an accurate representation of indirect and direct costs, please check Box A and complete Parts II and III on form DS-4513 and return the form to Michigan Department of Education, ATTN: Lori Schomisch, Office of Financial Management, P.O. Box 30106, Lansing, MI 48909 by June 11, 2004. **The deadline date for the return of the DS-4513 is crucial and no adjustment requests will be accepted after that date.**

Please be aware if your district recovered any of the costs classified as indirect costs on the R0418, the recovery must be reported in Part II. The recovery will be subtracted from indirect expenses, thus reducing the indirect cost rate.

3. Reporting Adjustments - Part 1 Adjustments: There are categories of expenditures that have been classified as direct costs on the preliminary R0418 that may include indirect expenses. There may also be direct costs that include expenditures that should be excluded. Fiscal audit fees, for example, can be considered indirect costs if the audit performed provided benefit for all programs and the fees were not charged to or identified with any specific program. Interest expenses are an example of costs that should be excluded from direct costs. Use form DS-4513 to report additions to and/or subtractions from restricted indirect, unrestricted indirect and direct costs.

The proportionate amount of time a superintendent has spent performing “service functions” is another example where the Report R0418 may not accurately reflect indirect costs. Often, in smaller organizations, the Chief Executive Officer performs duties more consistent to those allowed in the restricted indirect cost pool. If this is the case within your organization, the costs of the Chief Executive Offices associated with accounting, auditing, budgeting, personnel, purchasing, employee relations, etc., can be included in your restricted indirect cost pool. Most costs of the superintendent’s office can be included in the unrestricted indirect cost pool. Time studies must support an allocation to the restricted indirect cost pool; and if more than 50% of the Chief Executive Officer’s or their administrative support’s time is allocated, documentation supporting the percentage used must also be provided.

When determining how an expenditure should be classified, it may be helpful to ask the following questions:

- A. Can the costs be identified specifically with one program or activity? If so, the costs are considered to be **direct costs**.
- B. Do the expenditures pertain to:
 - 1. The school board,
 - 2. Contributions or donations, or
 - 3. Entertainment?If so, the expenditures are considered **unallowable**.
- C. Do the costs relate to:
 - 1. Capital outlay,
 - 2. Interest or debt service,
 - 3. Judgements,
 - 4. Fines or penalties,
 - 5. Bad debts,
 - 6. Election expenses,
 - 7. Food for food service.If so, the costs are considered to be distorting and are classified as **excluded costs**.
- D. Do the costs benefit all programs in general and cannot be readily identified with any program? If so, the costs are **unrestricted indirect costs**.
- E. Subtract from the unrestricted indirect costs any expenditures related to Operations and Maintenance and the Chief Executive Officer’s immediate office, including any Deputies or similar offices and their immediate support staff. The remainder is the value of **restricted indirect costs**.

Please note that many of the expenditures can be considered either direct, restricted indirect and/or unrestricted indirect, dependent upon the nature and the treatment of the costs. However, under no circumstance may a cost be considered both direct and indirect.

4. Provide Documentation to Support the Classification: It will be necessary to provide a schedule to support any adjustments. Under General Administration, for example, if time studies support that the superintendent spends 10% of his/her time in accounting and budgeting service functions, document the expenditures associated with the superintendent and how the expenditures are prorated between restricted indirect, unrestricted indirect and direct costs. Space is provided on page 2 of DS-4513 for this information.
5. Part II – Adjustment for Allocated Costs: One of the basic guidelines of the U.S. Department of Education’s Cost Principles for State and Local Governments is that indirect cost(s): “Not be allocable to or included as a cost of any other Federally financed program in either the current period or a prior period.” If any of the amounts included in the indirect costs represented on the R0418 or in your adjustments on the DS-4513 can be attributed to a specific program or activity, these amounts cannot be part of the indirect cost pool. You must report these costs in Section 2, Adjustment for Allocated Costs. These costs will be subtracted from the indirect cost pool (the numerator of the ratio) and added to the direct cost pool (the denominator of the ratio).
6. Carryforward Adjustment: The carryforward adjustment is calculated in MDE’s indirect cost database. It is not necessary to calculate the adjustment manually. This section is provided for information purposes only.

After completion of the DS-4513, the totals of the columns will be used to adjust the Form B data to identify restricted indirect, unrestricted indirect and direct costs in 2002-2003. The adjusted numbers will then be transferred to the indirect cost rate carryforward computation. If you district did not negotiate a rate for 2002-2003 or negotiated a zero rate, no carryforward adjustment will be allowed. The fixed carryforward will be zero, and the adjusted indirect costs will be the same as indirect costs as adjusted by the DS-4513.

The carryforward calculation is meant to adjust the current indirect cost rates by amounts over or under recovered in the second preceding year. It compares the actual direct cost base to the estimated direct cost base and the actual indirect costs to the estimated indirect costs. The amount of over or under recovery from 2000-2001 remains static and is included in the calculation. Adjustments are made to the indirect cost pool for the 2004-2005 to increase or decrease the current rate accordingly.

7. Forward the forms to the Department of Education: Upon completion, please forward form DS-4513 and supporting worksheets to:

Michigan Department of Education
Office of Financial Management
ATTN: Lori Schomisch
P.O. Box 30106
Lansing, MI 48909

Completed forms are due on or before June 11, 2004. You will be notified of your final

indirect cost rates by the Department. The preliminary rate may be utilized until such time as notification of the final rate is received.

Other Information:

1. Michigan schools indirect cost rates are “fixed” rates, meaning the rates are based upon previous year’s activity and a carryforward amount is included in the calculation to adjust the rates for actual results. While the calculation for the carryforward is cumbersome, it is necessary to comply with U.S. Department of Education requirements.
2. Records and documentation supporting the indirect cost proposal must be retained for a period of five years after the last day of the fiscal year to which the proposal applies.

Questions or Comments:

Your questions and concerns regarding indirect cost rates are welcome. Please contact Lori Schomisch at (517) 335-0539 or e-mail at schomischl@michigan.gov.